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Regional Technical Coordinator
Southeast Region

Assistant Chief Counsel (Income Tax & Accounting)
CC:IT&A:01

Technical Coordination Report Submitted By:
Ms. Sherry York
District: Ft. Lauderdale

Recommendation: Issue a revenue ruling or revise the regulations to clarify who is considered to be the "payor" when corporate earnings are distributed to third parties.

The technical coordination report identifies a situation in which an automobile dealership directs that commissions earned by it on the sale of extended warranty contracts be paid to the dealership's shareholders. Because the dealerships are corporations, no information returns are issued to them pursuant to section 1.6041-3(c) of the Income Tax Regulations. The extended warranty company is not issuing any kind of Form 1099 to the individuals to whom it makes the direct payments.

The technical coordination report observes that the phrase "makes payment in the course of such trade or business" as used in section 6041 of the Code is not defined in the regulations or in revenue rulings. Also, section 6042(b) and the regulations thereunder contain a special rule that requires the reporting of payments that may be dividends. Consequently, there appears to be some leeway to require information reporting by the warranty company.

We believe that existing authorities do not require the company that issues the extended warranty to report the payments made to the automobile dealership's shareholders.

Section 1.6041-1(f) of the regulations provides guidance in determining when and to whom a payment is deemed made. Generally, the deemed payment rule mirrors the constructive receipt rule.

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In addition, section 35a.9999-3, Q and A-1, of the Temporary Employment Tax Regulations provides guidance in determining which person is considered the "payor" when amounts are disbursed by an agent. Paying agents are not considered to be payors, but collecting agents are considered payors. Section 35a.9999-3 was promulgated to provide guidance in connection with backup withholding; however, it is also authoritative with respect to and to the extent it deals with information reporting issues. (We believe Rev. Rul. 73-232, 1973-1 C.B. 541, is no longer a valid statement of Service position in light of section 35a.9999-3, Q and A-1, to the extent the ruling requires a so-called "fiscal paying agent" to issue Forms 1099.) The extended warranty company is not acting either as a paying agent or a collecting agent in the situation described in the materials submitted with the technical coordination report.

We do not think the special rule contained in section 6042(b)(3) of the Code and the regulations thereunder has any application except in cases in which distributions intended to be dividends are involved. Senate Report No. 1881, 87th Cong., 2nd Sess. (1962) states: "... where a payor is unable to determine whether a payment is a dividend, he is to include the entire amount as a dividend for reporting purposes." 1962-3 C.B. 707, 828. In addition, the Technical Explanation of the Bill, in discussing section 6042(b)(3) states: "... if a corporation is unable to determine what portion of its distributions to its shareholders during the calendar year is paid out of earnings and profits, the total amount of the distributions must be treated as a dividend." 1962-3 C.B. 842, 1029.

While the scope of section 6042(b)(3) of the Code may be broader than the example given in the Technical Explanation, we do not believe that provision can be used to require reporting by one taxpayer of a payment that, if made directly by a second taxpayer, might be a dividend. This is particularly true when the payment was originally intended as a commission.

In the situation described in the technical coordination report, which is the same as the situation in a request for technical advice currently pending in our office, all of the commissions are deemed paid to the corporation that earned them. We do not think we can require the extended warranty company to issue Forms 1099 directly to an automobile dealership's shareholders. However, the dealership (as payor) would be required to report (either as commissions or dividends) the amounts disbursed by the warranty company to the shareholders.

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A revenue ruling that sets forth the Service's position using the factual situation presented in the technical coordination report would be helpful both to taxpayers and to our examining personnel in resolving issues in this area. Therefore, we intend to recommend the issue for publication as a revenue ruling.

We appreciate Ms. York's interest and initiative in submitting this report. Copies of this memorandum are enclosed for the Regional Technical Coordinator, the District Technical Coordinator, Ms. York, and other interested parties.

(signed) Glenn R. Carrington

Glenn R. Carrington
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(Income Tax & Accounting)